Pearson FAQs

What's does the resolution call for?

- The proposal requests that the board immediately conduct a thorough business strategy review of Pearson including education commercialization and its support of high stakes testing and low-fee private schools and to report to shareholders within six months.
- The proposal encourages the board to focus on the long-term growth of the corporation by shifting the company away from educational policies that create unnecessary financial and reputational risks.

Why now?

- Pearson faces serious competitive and reputational challenges to its core educational businesses in the US which demand a comprehensive re-evaluation of the company's business strategy.
- The company is suffering a crisis of confidence with four profit warnings in four years and shares down over 40% since last year's shareholder meeting (see ***How has Pearson performed in recent years?***).
- The board's response to this crisis, a new cost-cutting initiative announced in January, marks the second restructuring plan of CEO Fallon's three and a half year tenure; pushes back a long-awaited return to profitable growth by an additional two year; and fails to address the deeper structural trends that are undermining the economics of Pearson's business model in its main market (see ***What's gone wrong at Pearson?***).

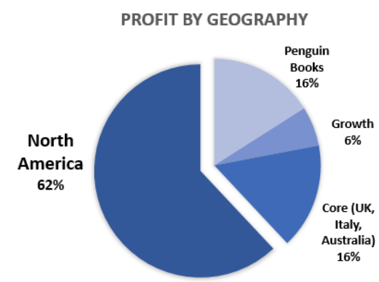
How has Pearson performed in recent years?

- After posting strong growth in the five year period ending 2011, Pearson has since stagnated, failing to consistently grow revenue, profits and suffering from a slumping share price.

		2012	2013	2014	2015
Total Shareholder Returns*	*Absolute*	2.1%	17.2%	-7.6%	-33.8%
	+/- FTSE 100	-7.8%	-1.5%	-8.3%	-32.5%
Revenue (in GBP millions)**		4,959	5,069	4,874	4,468
Operating Income (in GBP millions)**		589	577	432	389
Return on Invested Capital***		9.1%	5.4%	5.6%	5.8%

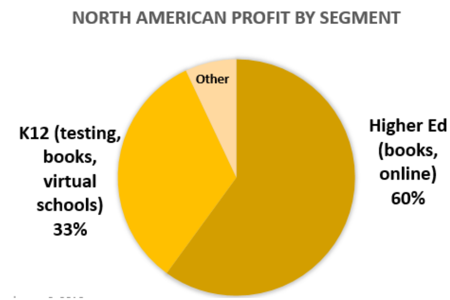
* As reported by Morningstar, ** as reported by CapitalIQ, *** as reported by Pearson

If Pearson is a UK-listed company, how important is the US business to Pearson?



- Following the recent sale of *The Economist* and the *Financial Times*, the US accounts for two thirds of Pearson's business. Pearson is the world's largest education company by revenue and is described as the most powerful force in US education by Fortune Magazine.

How important is US K-12 to Pearson's business?



- K-12 education comprises a third of the US business, or around 20% of total company profits; 8% is from testing and courseware, respectively, and the remainder from virtual schools. In higher-education, Pearson is the largest supplier of text books and a major developer of online courseware.

What's gone wrong at Pearson?

- While Pearson insists its business has been hit by one-off factors and broad economic challenges, a number of analysts point to strategic missteps and underlying problems in the company's business model and competitive positioning.
- **Mishandling of K-12 testing business**: Pearson's investment in high-stakes testing, in particular Pearson's role in the Partnership for Assessment of Readiness for College and Careers consortium (PARCC), has created unprecedented reputational damage and political backlash for Pearson. The promised growth has not materialized as the PARCC consortium has unraveled while Pearson's brand has become toxic, putting various K-12 testing contracts at risk and threatening contagion to its K-12 courseware business.
- **Further risks to existing strategy from recent passage of Every Student Succeeds Act:** ESSA, which replaced No Child Left Behind last year, is likely to have a large impact on Pearson's market. It decentralizes contracts back to the States and broadens the range of stakeholders involved in the approval process making it harder for Pearson to win testing contracts unless it

rebuilds its brand and relationships with key stakeholders, including teachers. At the same time States struggling to balance tight budgets will no longer be required to subscribe to expansive testing programs like Pearson's PARCC. States will be free to select more cost-effective assessments and support programs.

- **Cost pressures in higher education:** A growing unwillingness of US higher educational students to pay high prices for text books and increasing use of book rentals and open-source options, including Google and Apple has analysts drawing parallels between Pearson's text book business and the bygone era of CDs. As one analyst put it: "[T]ogether with pervasive wireless broadband [this will] rip up the established order in educational publishing" (Jefferies).
- **Pearson's overall model of commercializing education under threat:** As Deutsche Bank analysts note, the **"**Market is becoming more fragmented and competitive with for-profit providers like Pearson facing increasing competition from new entrants including many non-profit providers."

What do analysts think?

- "[The job cuts and restructuring] looks more of an exercise in delaying the inevitable than tackling the true causes of their deep-rooted problems" (Librium Capital)
- "It's another three years of minimal growth even on their optimistic scenario. There's still no sign of the long-term vision of education growth coming through." (Panmure Gordon)
- "This leaves investors grasping at rather hollow assurances that things will get better" (Macquarie)
- "A turnaround is unlikely to be a simple as embarking on another cost-cutting plan" (Kepler Cheuvreux)
- "We find it difficult to build confidence that [the new restructuring] will deliver" (Barclays)

Have investors previously raised concerns at the annual shareholder meeting?

- At each of the past two annual meetings, the AFT and/or other proponents of this resolution have raised concerns to CEO Fallon over Pearson's reliance on high-stakes testing and low-fee private schools.